Caltex submission to Queensland Parliament Impact of Petrol Pricing Select Committee

December 2005

(This version of the submission has been edited to remove commercially sensitive information and may be publicly released)

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Caltex's submission is in two parts: a main submission that addresses terms of reference a, d and g, which may be published; and a confidential appendix, which is confidential and not for publication or dissemination outside the committee or its secretariat.

Background - Caltex structure and operations

Caltex Australia Limited is Australia's leading refiner and marketer of petroleum products under the Caltex, Ampol and Bogas brands. Caltex is the only major refiner and marker listed on the Australian Stock Exchange. Chevron Corporation of the US is a 50% shareholder but Caltex is not a subsidiary and all decisions are made by Caltex's Australian board and management. Caltex is engaged in refining and marketing only and has no exploration or production interests, nor any overseas refining or marketing operations. Caltex has two refineries, in Sydney (Kurnell) and Brisbane (Lytton) and as at 31 December 2004 owned or leased 577 service stations within a network of 1813 Caltex, Caltex Woolworths and Ampol branded service stations. Caltex has about 3000 employees.

There are 366 Caltex, Caltex Woolworths or Ampol branded service stations in Queensland. These sites are operated by various entities as shown in Table 1 below.

Table 1

OPERATION (FUEL SALES)	METRO	COUNTRY
CALTEX EMPLOYEE OR COMMISSION AGENT	11	2
FRANCHISEE	66	20
WOOLWORTHS COMMISSION AGENT	26	3
INDEPENDENTLY OPERATED (INCL. WOOLWORTHS EMPLOYEE OPERATED*)	63	175
TOTAL SITES	166	200

Data: November 2005, includes only sites accepting Starcard (most sites)
* Woolworths web site lists 60 employee-operated sites

Various pricing arrangements operate at these types of sites:

- Caltex operates a small number of sites, mainly with company employees, as shown in the first row of the table below. At these sites, prices are set by Caltex or at Caltex's direction.
- About a quarter of sites are operated by Caltex franchisees. Under a Caltex franchise, fuel is purchased by the franchisee at Caltex's ruling wholesale price, the Caltex Reference Price (CRP). A franchisee may also be eligible for price support to help meet local competition, which effectively reduces the franchisee's wholesale price.
- Woolworths commission agents may be sites with Caltex employees or franchisees acting as commission agents for the sales of Woolworths fuel. Caltex or franchisees operate the convenience stores. Woolworths determines the fuel prices.
- Independently operated sites (which include sites with Woolworths employees) purchase fuel at wholesale from Caltex or its resellers (distributors) for resale. Prices are set by the independent operators. Fuel from Caltex is priced either under a national contract (eg Woolworths - terms are confidential) or at the CRP less a negotiated fixed discount.

  Where retailers are not directly supplied by Caltex but by a Caltex branded reseller, the price to the reseller is based on CRP less a fixed discount and it is believed the price to the retailer is also based on the CRP less some fixed discount (if any) offered by the reseller. This formula has the advantage to the retailer of being transparent as the CRP is available via dial-up, so allowing invoice prices to be checked easily.

In Queensland, Caltex is a bulk wholesale supplier and licenses its Caltex and Ampol brands for use at service stations. Fuel may be distributed directly to service stations from seaboard terminals by Caltex or distributed by branded resellers, which may have 100%, 50% or zero Caltex ownership. Caltex ultimately is responsible for the wholesale price from 100% equity resellers to service stations, although day to day operation is by the reseller. Caltex does not set prices from 50% or zero equity resellers and is prohibited by law from doing so. Reseller arrangements are summarised in Table 2 below.

Table 2

Caltex controlled	Auer Petroleum	Bundaberg	25% of volume
	Caltex Far North Queensland	Cairns	
	Petro Fuel Pty Ltd	Darling Downs, Emerald & Roma	
50% equity	South East Qld Fuels Pty Ltd	Rocklea	75% of volume
Not Caltex controlled	Bonick Pty Ltd	Mundubbera	
	Central Queensland Petroleum Pty Ltd	Gladstone	
	Country Petroleum Pty Ltd	Dalby	
	Crokers Fuel & Oil Pty Ltd	Mackay	
	Hawkins Road Transport	Wynnum Central	
	IJ BF KJ & JI McClintock	Maryborough	
	JL Keen	Nikenbah	
	Tropic Distributors Pty Ltd	Townsville	
	W H Phipps & Coy	Taroom	

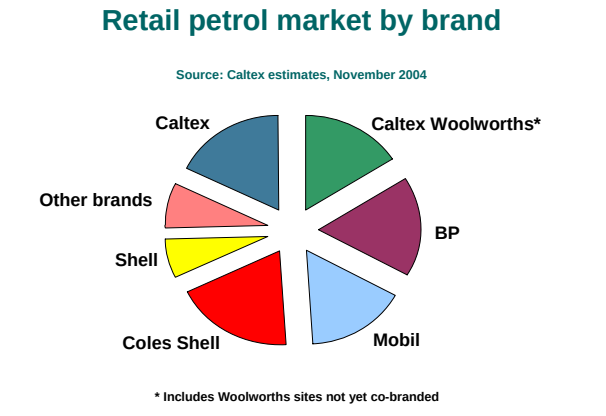
Approximately 4300 ML of petrol was sold in Queensland in 2004. Caltex supplied about 1200 ML this volume, representing about 27% of all petrol sold.

Caltex supplies petrol from bulk storage terminals it operates at Lytton in Brisbane and at Gladstone, Mackay and Cairns. Petrol is supplied from joint venture terminal with Shell in Townsville. There is ethanol storage at Caltex's Cairns terminal.

Caltex operates a refinery at Lytton in Brisbane which supplies about 55% of Queensland's transport fuel requirements (petrol, diesel and jet fuel).

For information and comparative purposes, Chart 1 indicates the split of the retail market share by brand across Australia. Brand market share indicates how many sites display a company's brand, not who operates the sites. Very few branded sites are operated by the four refiner-marketers. Sites may be operated by the companies that own the major brands, franchisees, commission agents or independents. (Note that all Woolworths sites have now been co-branded.)

Chart 1



Background – fuel pricing

Factors underlying Australian petrol prices

The following information is extracted from *Petrol Pricing - the Plain Facts* on www.caltex.com.au. The information is relevant to Australia as a whole as well as Queensland.

There are four major elements that affect the prices we pay for petrol in Australia, the first two of which have directly affected the higher fuel prices seen the past year:

1. the price of petrol from Singapore refineries in US dollars (which is charted daily by the Australian Institute of Petroleum)
2. the value of the Australian dollar relative to the US dollar – when the value of our dollar falls, this increases petrol prices
3. Australian Government excise and GST and state government subsidies
4. margins within Australia for storage and distribution, wholesaling and retailing.

Prices for petrol from Australian refineries are not based on the actual cost of imported petrol or the crude oil that is refined into petrol. Instead, the ex-refinery price of petrol is based on an "import parity price" calculation. This is a theoretical calculation based on the Singapore market price for petrol, adjusted for Australian fuel standards and freight to Australia. The import parity price is not regulated but instead determined by market forces.

The reason Australian petrol prices follow Singapore market prices is that Australian refineries must compete against petrol imports (overall, about 17 percent of Australia's petrol was imported in 2004) and Singapore is a major source of petrol for importers.

Changes in Singapore petrol prices or Australian/US dollar exchange rates typically take one to two weeks to flow through into either increases or decreases in pump prices. These changes are often masked by weekly cycles in pump prices in major capital cities.

Differing levels of competition affect petrol and diesel prices in the Australian retail market. Petrol prices are often discounted in major capital cities – and heavily – as a result of intense competition for customers. Diesel is not discounted to the same extent as petrol prices because much less is sold at retail and therefore service station dealers concentrate on petrol discounting to drive overall fuel sales volumes and associated shop sales.

The bulk supply price for refined products into terminals is known in oil industry jargon as the "buy-sell price" and is negotiated every 6 months on a bilateral basis between Australian refiners and potentially other Australian bulk suppliers, either for sale or purchase. Imports are negotiated on a cargo by cargo basis.

Tables A1 and A2 (confidential attachment) show buy-sell price calculations for petrol and diesel for a day in second half 2005, which are based on the applicable daily Singapore prices.

Tables A3 and A4 (confidential attachment) show the calculation of Caltex's ruling wholesale price ("Caltex Reference Price" or CRP) for petrol and diesel, which are the basis for pricing to service stations and resellers. A discretionary after sale rebate off the CRP may be provided to franchisees to help them meet local price competition; wholesale prices to resellers and non-franchised retailers are generally discounted at time of purchase.

The purpose of these tables is to show that pricing of petrol is not arbitrary or particularly complex, although necessarily confidential. Prices are related to an import parity price calculation and closely follow movements in international petrol prices through the linkage to Singapore prices.

A terminal gate price (TGP) is also posted at each Caltex terminal and available on the Caltex web site, www.caltex.com.au. This is the spot price for a road tanker load (about 42,000 litres) of unbranded bulk petrol supply from the Caltex terminal for cash. The TGP calculation is similar to

buy-sell except it uses a 7 day rolling average of Singapore prices and exchange rates, is adjusted only twice weekly, and includes a terminalling cost and competitive wholesale margin for the particular terminal location.

Retail and wholesale margins

Caltex publishes historical data for franchised sites on its website, shown in cents per litre. This data can be used to deduce average franchisee margins per month, broken down by state and metropolitan/regional area. The data can be found at http://www.caltex.com.au/pricing_his.asp.

To calculate the average franchisee margin in metropolitan and regional areas in each state: average franchisee margin = retail (pump) price – freight – wholesale price + state subsidy of 9.2 cpl. The following data is for September 2005:

Table 3

Cents per litre	VIC		NSW		ACT	QLD	
	City	Country	City	Country	City	City	Country
1 Retail (pump) price	129.0	***	129.6	133.4	134.8	120.8	125.1
2 Freight	0.7	***	0.8	2.6	2.2	0.7	1.0
3 Wholesale price	125.2	***	125.6	126.6	128.3	126.5	128.9
4 Terminal gate price	123.1	***	125.7	***	***	125.3	***
5 Net excise (excl GST)	37.7	***	38.1	36.6	38.1	38.1	38.1
6 GST	11.7	***	11.8	12.1	12.3	11.0	11.4

Cents per litre	SA		WA		Tas		NT	
	City	Country	City	Country	City	Country	City	Country
1 Retail (pump) price	132.2	***	129.3	131.6	135.3	***	***	***
2 Freight	0.5	***	0.5	1.0	0.7	***	***	***
3 Wholesale price	128.7	***	125.8	127.6	129.0	***	***	***
4 Terminal gate price	127.5	***	127.4	***	126.9	***	128.4	***
5 Net excise (excl GST)	38.1	***	38.1	38.1	36.2	36.2	37.0	***
6 GST	12.0	***	11.8	12.0	12.3	***	***	***

*** insufficient data

Responses to terms of reference

Caltex is not able to make responses to all terms of reference because only some are within its area of expertise. The preceding discussion bears upon various terms of reference whereas the following comments are more specific to each term.

(a) Consider the extent to which current petrol prices increase the competitiveness of alternative fuels such as E10

Caltex has sold about 400ML of E10 Unleaded Petrol (E10) since 1996 through its Bogas branded sites in central and northern NSW, initially by 50%-owned reseller Bowen Petroleum and now through 100%-owned reseller Access Energy. There are currently 27 sites selling E10, which will be progressively rebranded to Caltex. E10 is blended at Caltex's Newcastle terminal and most ethanol is purchased from Manildra group of companies. An upgrade of ethanol storage facilities at the Caltex Newcastle terminal is under way.

There are 12 Caltex and Ampol branded service stations selling E10 in Far North Queensland from Ayr to Cairns, and supplied by Caltex or its branded reseller Tropic Petroleum. Four sites were part of a trial operated by Caltex from May 2003, which was successfully concluded earlier this year. Following the trial, E10 is now one of the range of Caltex quality petrols. As well as retail sales, sales of E10 to commercial accounts are developing. The E10 is blended at the Caltex Cairns terminal through a new facility built in 2003, with ethanol supplied by CSR Limited from its Sarina plant (via Melbourne for dehydration).

E10 supply has been extended to Caltex retailers in South East Queensland via two Caltex resellers, Petro Fuel Pty Ltd and Independent Fuel Supplies. Petro Fuels' network has 11 sites selling E10 in regional South East Queensland under the Caltex brand. The Petro Fuels business has recently been acquired by Caltex.

Biodiesel blends (B20) are supplied to Newcastle City Council and Solo Waste (NSW several NSW Central Coast) customers under commercial contracts. Biodiesel blends (B5) are supplied to several Adelaide bus companies under commercial contracts. Caltex is receiving numerous commercial inquiries for supply of biodiesel blends.

A retail trial of B5 by Caltex-owned reseller Access Energy started in September 2005 at three sites in Hexham, Tamworth and Quirindi.

Caltex supports the commercial development of biofuels. Caltex is committed to the Australian Government's biofuels production target of 350ML annual sales of ethanol or biodiesel to the Australian market by 2010 and will play an appropriate part in helping to achieve that target, subject to the following:

- consumers must feel confident in using petrol blended with ethanol
- ethanol needs to be supplied reliably on a year-round basis
- supply of ethanol must be priced competitively.

Caltex intends meeting its 2010 target commitment through controlled expansion of biofuel blends including blends of biodiesel and ethanol. Any expansion beyond the 2010 target will be based on commercial considerations, including competition between all forms of refined and alternative fuels to meet consumer demands.

The following chart shows a typical build-up of wholesale and retail petrol prices from the Singapore price. A very similar build-up would apply to diesel.

Chart 2

Petrol v ethanol prices

	Case 1	Case 2
Singapore petrol price (US$/barrel)	65	40
Landed price (incl. quality premium) plus terminalling cost, wholesale margin and freight (A cpl)	68	48
plus retail margin	3	3
plus excise	38	38
less retail subsidy	8	8
plus GST	10	8
Total retail price A cpl	111	89
Note: wholesale price + tax (excl GST) Acpl	106	86

Petrol price decreases 0.8 cpl per 1 US$/barrel Singapore price decrease (159 litres/barrel)

Ethanol wholesale prices (excluding GST) estimated 75 cpl (high case), 60 cpl (low case). Petrol/ ethanol price difference must include allowance for freight and E10 infrastructure cost recovery

At an assumed Singapore petrol price of US$65 per barrel, the resultant pump price (average over a week) is 111 A cpl. At US$40 per barrel, the pump price is 89 cpl. Corresponding wholesale prices (excluding GST) are 106 A cpl and 86 A cpl.

From the viewpoint of a theoretical service station faced with the choice of purchasing E10 or straight petrol, the wholesale petrol price is 106 cpl and ethanol about 75 cpl, a difference of about 30 cpl, or 3 cpl in a 10% blend. In reality, the advantage is not so great as ethanol delivery is typically more expensive due to greater distance from the plant and an allowance needs to be made for amortisation of service station conversion costs for E10. Assuming these items come to 10 cpl, the cost advantage of E10 is about 2 cpl, quite significant compared with a typical Brisbane gross retail margin of about 3 cpl.

At low oil prices, the cost advantage of ethanol is reduced but the ex-plant cost of ethanol is also likely to be much lower, perhaps down to 60 cpl at low oil prices. It must be stressed these prices are purely indicative and are not intended to represent current Caltex negotiations. Nevertheless, the figures should give the committee a feel for the economics of ethanol blends.

Retail pricing strategy is for individual retailers to determine. Some can and do choose to discount E10, perhaps while building market share and possibly as a longer term strategy. Others may choose to price E10 the same as unleaded petrol but promote the higher octane of the E10 blend. These are legitimate competitive strategies and will also evolve as the market matures.

E10 therefore *may* reduce petrol prices but given the reduction of cost advantage with lower oil prices, government policy should not rely on E10 to reduce petrol prices.

(d) Consider the extent to which recent fuel increases could be moderated through enhanced domestic competition, including how the ACCC powers could be strengthened to deliver enhanced competition.

Response of Australian prices to international prices

With recent petrol price rises around Australia there have been allegations that retail prices are quick to rise when international prices rise and slow to fall when international prices fall. These claims are examined in this section.

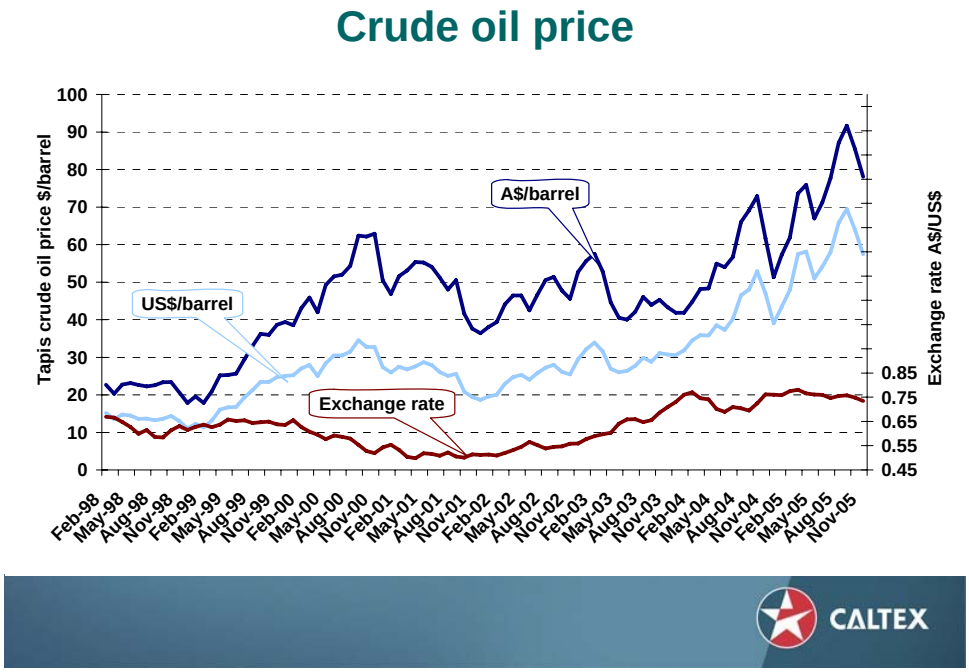
The ACCC has confirmed in Federal Parliament that its research showed Australian petrol prices to move closely in line with the international factors. ACCC representative Mr Cassidy stated, "We are generally satisfied that refined product prices in Australia have reflected international price movements. There are lags involved and we have had complaints in particular areas where prices do not seem to have come down by as much as they perhaps should have. We have looked into those cases and the answer in some of those areas is that, because of the lags involved, prices actually did not go up by as much as they probably could have initially. I am not saying it is a perfect correlation, either in time or space, but, as a general proposition, we believe that refined product prices in Australia are reflecting international refined product prices. Indeed, I have got a chart, which I will quite happily give you, that does show a very close correlation."[1]

Chart 3 shows the price of crude oil since 1998 in US$ and A$ per barrel (159 litres). Australian dollar crude oil prices were typically in the range A$40 to 50 from 2000 through to early 2004, although there significant downward and upward trends within this period and a rising exchange rate moderated the impact of US$ crude oil prices through to early 2004. Public consciousness of historical petrol prices relates to this period, under $1/litre in most states and under 90 cpl in Queensland. Since then, crude oil prices have risen by about A$40 per barrel or 25 cents per litre. It is this strong upward trend in crude oil prices, not refiner margins or wholesale or retail margins, that has been the main driving force in increasing petrol prices relative to the public's historical perceptions.

International price changes

Chart 3 shows crude oil prices since 1998 and Chart 4 shows the Singapore petrol price (MOPS95) over the same period. This is the price that is commonly used as a basis for setting petrol prices in Australia on the basis of an import parity calculation. The patter is similar to crude oil, with price typically in the A$50 to 60 per barrel range from 2000 to early 2004. A spike in March/April 2003 marks the Gulf War and another spike in September 2005 marks Hurricanes Katrina and Rita. From mid 2004, prices rise sharply due to underlying crude oil prices.

Chart 3



[1] Hansard, Senate Economics Legislation Committee, 17 February 2005, p.E30

Chart 4

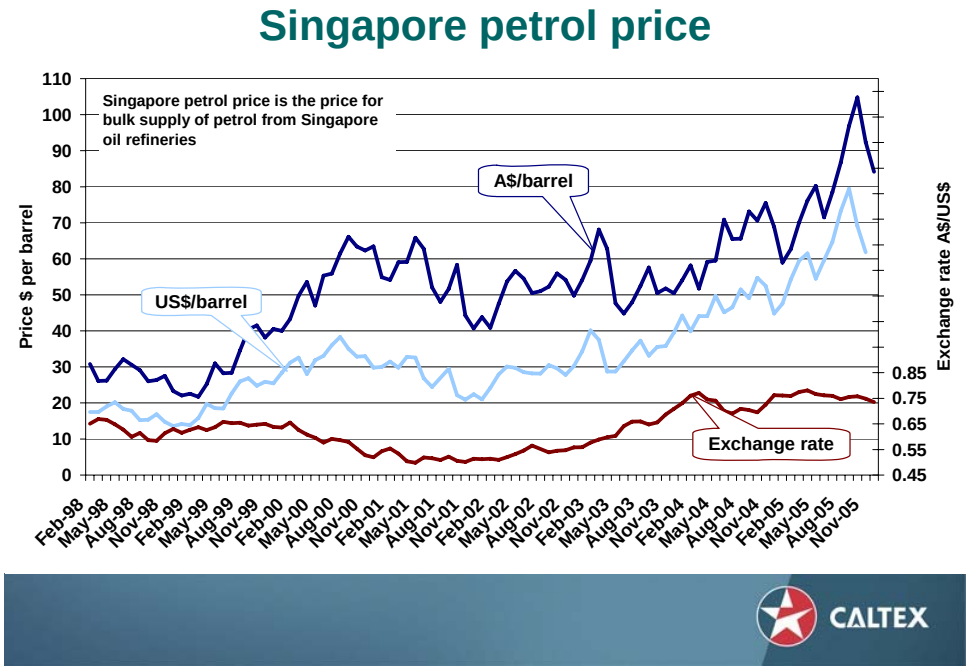


Chart 5 shows the Singapore diesel price (0.05% sulfur gas oil ie 500 ppm sulfur diesel) and appears very similar to the petrol price chart, although there are significant differences between petrol and diesel as shown on the next chart. Once again however, underlying crude oil prices are the driving force over longer (several months) time frames. (The shorter time period than the previous charts is because the particular low sulfur diesel price quote has only been available since 2001.)

Chart 5

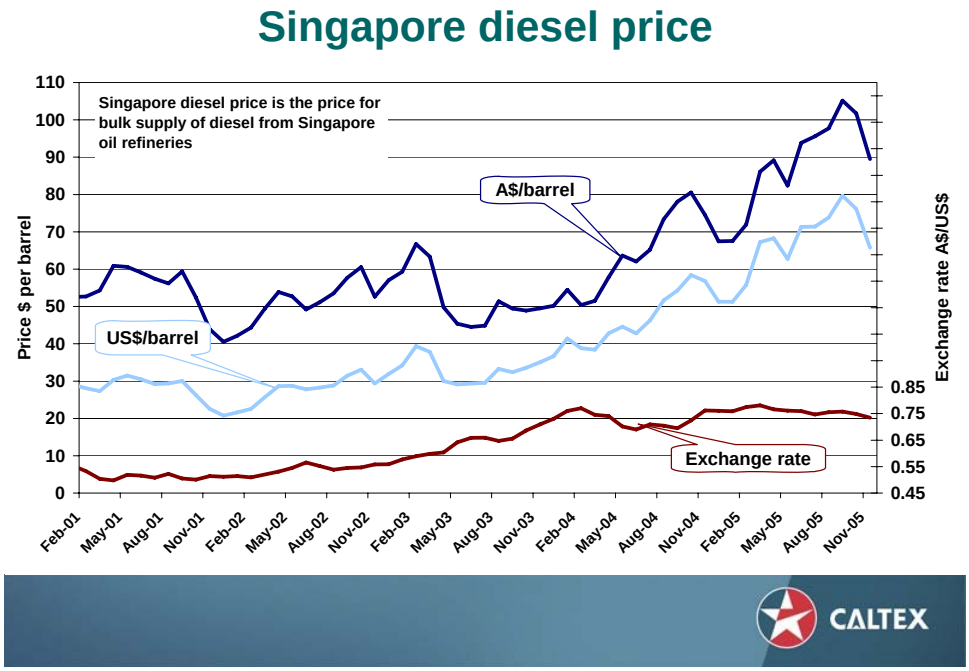
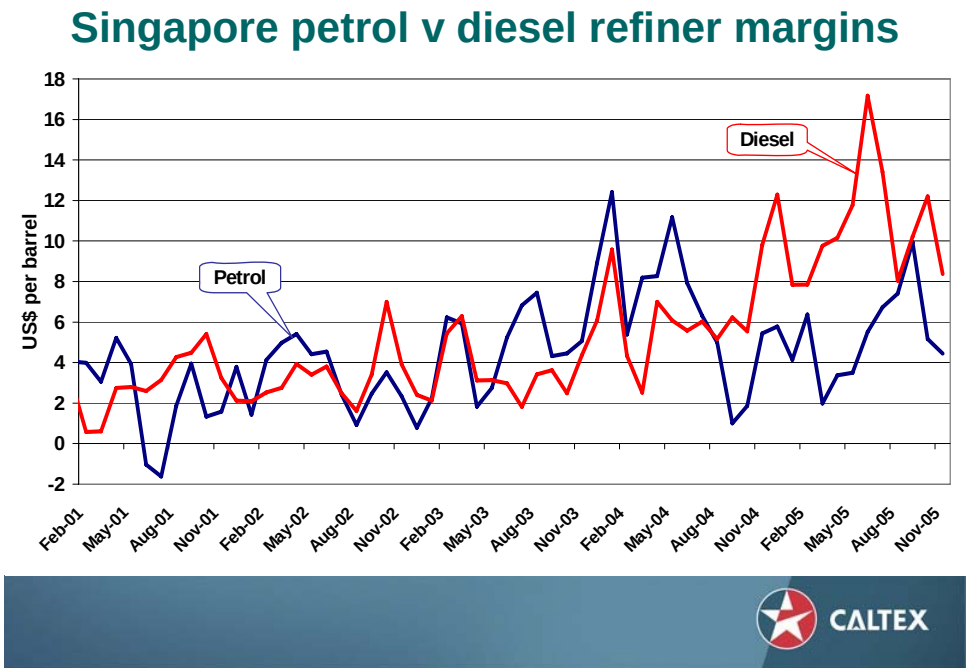


Chart 6 shows refiner margins for petrol and diesel. The refiner margin is the difference between the selling price of the product ex-refinery and the cost of crude oil, in this case the regional marker crude oil, Tapis (a low sulfur Malaysian crude oil).

Chart 6



It can be seen that the refiner margin for petrol has typically been in the range US$2 to 4 per barrel since 2001, with some significant excursions. From mid-2003, Chinese demand for petrol from fast-growing new car sales pushed up refiner margins until mid-2004 when demand controls applied by the Chinese Government eased petrol demand and as a result Singapore petrol prices. From 2Q2005, northern summer demand pushed up petrol refiner margins with Hurricane Katrina striking on 31 August. Margins quickly returned to more normal levels so that by the time of this submission, petrol margins had returned to the typical range. In other words, while petrol refiner margins are higher than early this decade, the increase is not significant in explaining the large increase in pump prices – that is mostly due to higher crude oil prices.

The diesel margin was typically in the US$2 to 4 range from 2001 to late 2003 but since then has shown a strong upward trend due to demand growth in Asia, with refinery supply constraints from time to time creating price volatility. The relativity of petrol and diesel refiner margins is an important factor in explaining the perception that “diesel use to be cheaper than petrol and now it’s dearer”. As the chart shows, petrol and diesel refiner margins (hence import parity price calculations) were similar from 2001 through to mid 2004 but have diverged on trend since then. This is due to differences in supply and demand in the Asia-Pacific region for the two products. It is also clear how supply and demand, not refinery costs (which are about US$2 to 3 per barrel) determine products prices.

Chart 7

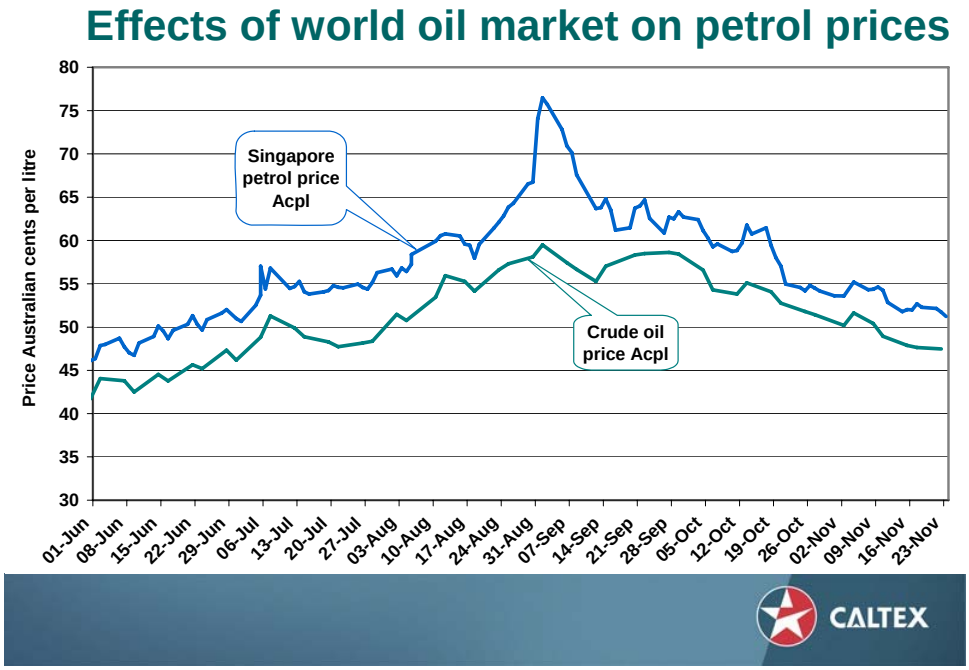
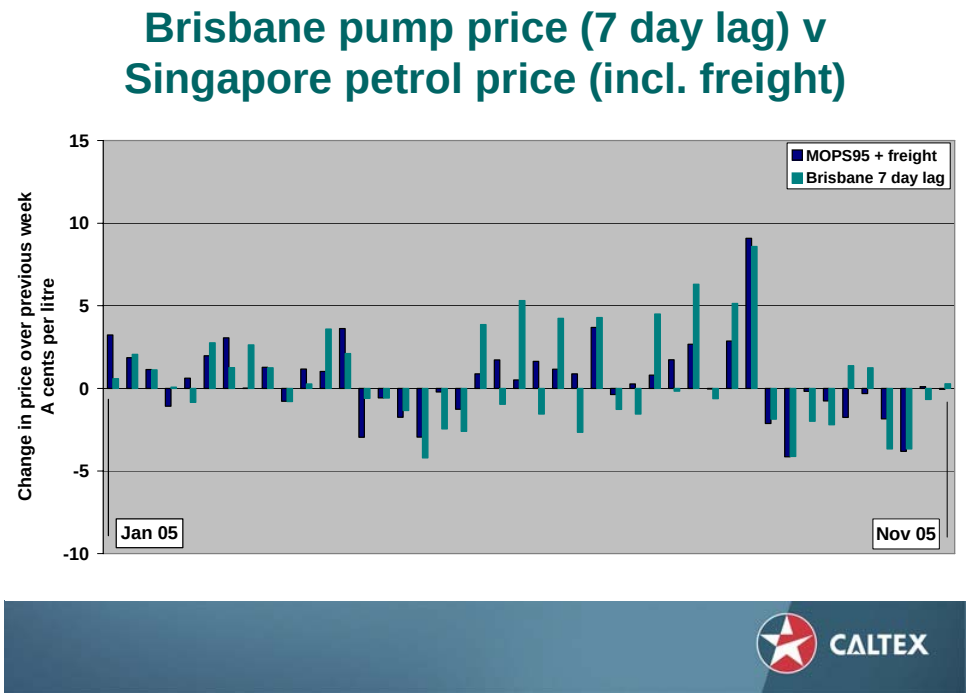


Chart 7 shows Singapore petrol price v crude oil price, both in Australian cents per litre (A cpl). The price spike caused by Hurricane Katrina is clear but so is the rapid decline almost immediately after the peak. Within two weeks, the price increase has completely dissipated, with refiner margins lower after than before the effects of the hurricane. It is worth noting that the petrol price shock reduced Australian petrol sales by 6.3% in September versus August, allowing Australia to meet the emergency measure imposed by the International Energy Agency that all member countries cut net oil consumption by at least 4%. Without the effect of higher prices, Australia may have had to impose rationing but the Australian Government assessed correctly that higher prices would curb demand sufficiently.

Chart 8 is the first of a set of charts considering changes in pump prices in response to Singapore petrol price changes. A criticism commonly levelled at oil companies by the public is that petrol prices are quick to rise but slow to fall in response to international prices. This chart considers the correlation of Brisbane pump prices (weekly average across all brands) one week after a change in the Singapore price (MOPS95) plus freight (since the calculated import parity price includes freight to Australia). The one week lag can be explained by wholesale pricing formulas (Caltex uses a 7 day rolling average to smooth out daily MOPS95 fluctuations) and stock turnover at metropolitan sites.

Chart 8



The chart shows changes in pump and Singapore prices are reasonably correlated (with a one week lag) and the amplitudes also, but not on a week by week basis. It is clear that while the correlation is quite strong, other factors can greatly affect the correlation on a week by week basis, including weekly competitive price cycles.

Chart 9

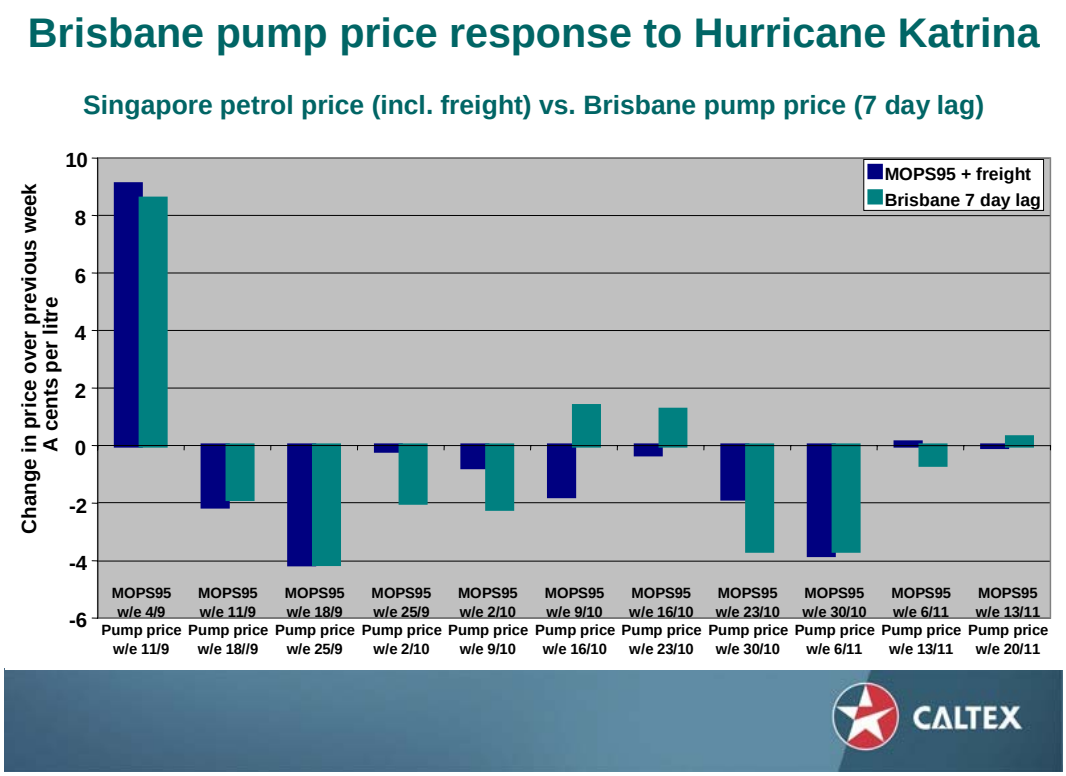


Chart 9 shows a shorter, more recent period from the previous chart. It can be seen that the Singapore petrol price (plus freight) increased 9 A cpl in the week Katrina struck and the Brisbane pump price rose on average about 9 A cpl the following week. A week later, the Singapore price fell 2 A cpl and the Brisbane price (a week later) by the same amount. The same pattern occurred the following week. The very clear message from the chart is that Brisbane pump prices increased and decreased almost exactly in line with Singapore prices in both directions.

Chart 10

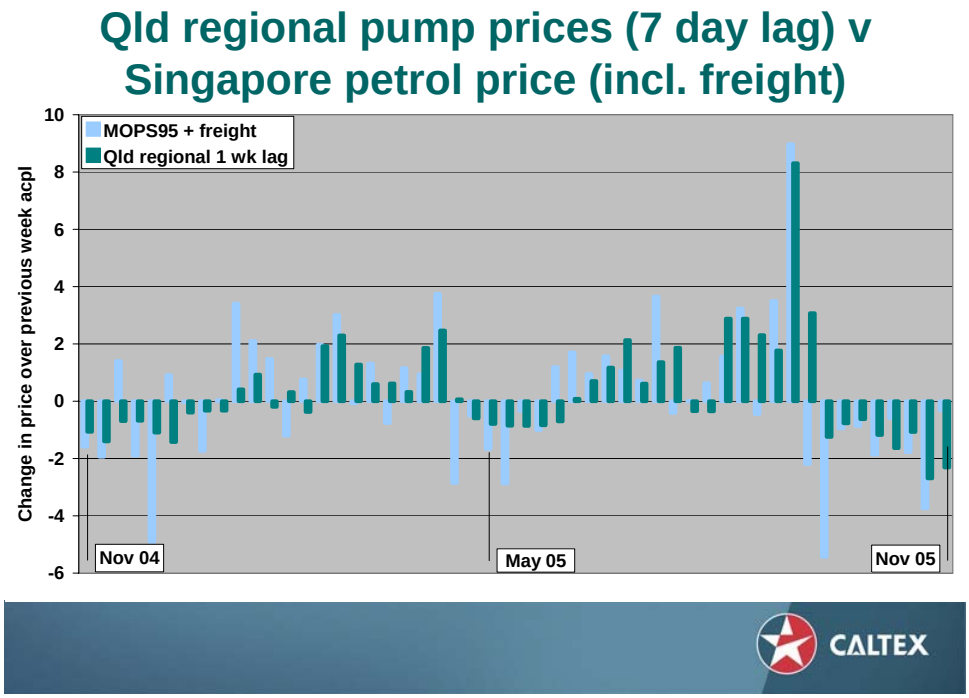


Chart 10 shows the correlation of average Queensland regional prices against Singapore prices. As for Brisbane, the correlation is quite good allowing for a one week lag in pump prices but the amplitude of the pump price response is generally less than Singapore prices. In other words, regional prices follow Singapore prices but neither rise nor fall to the same extent.

Chart 11

Regional Qld pump price response to Hurricane Katrina

Regional average pump price (7 day lag) v Singapore petrol price (incl. freight)

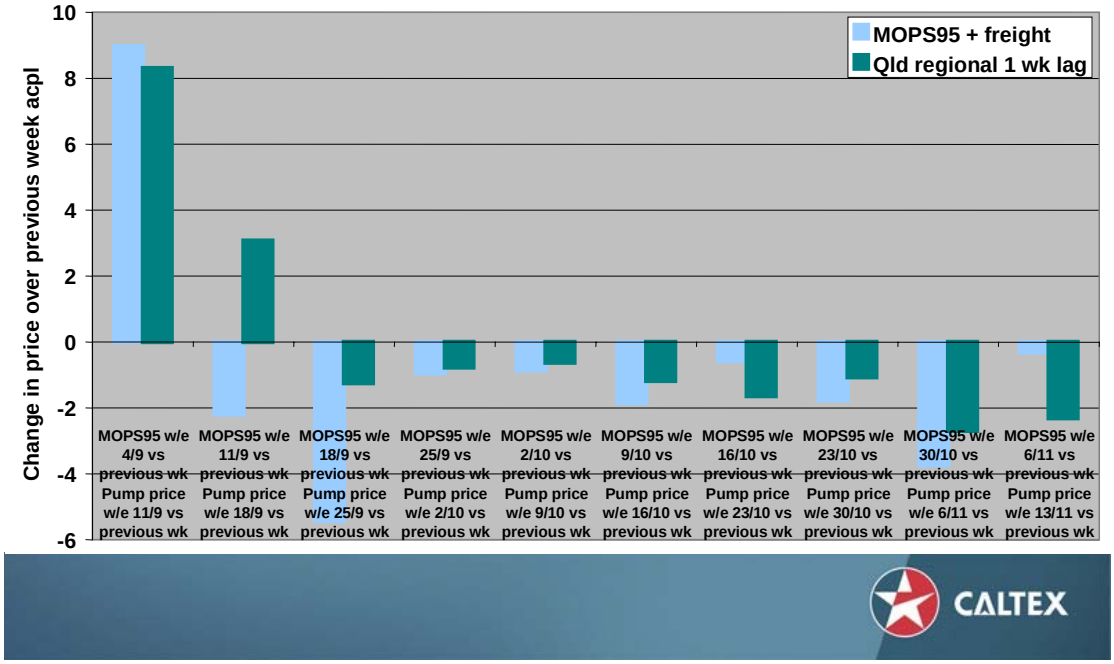
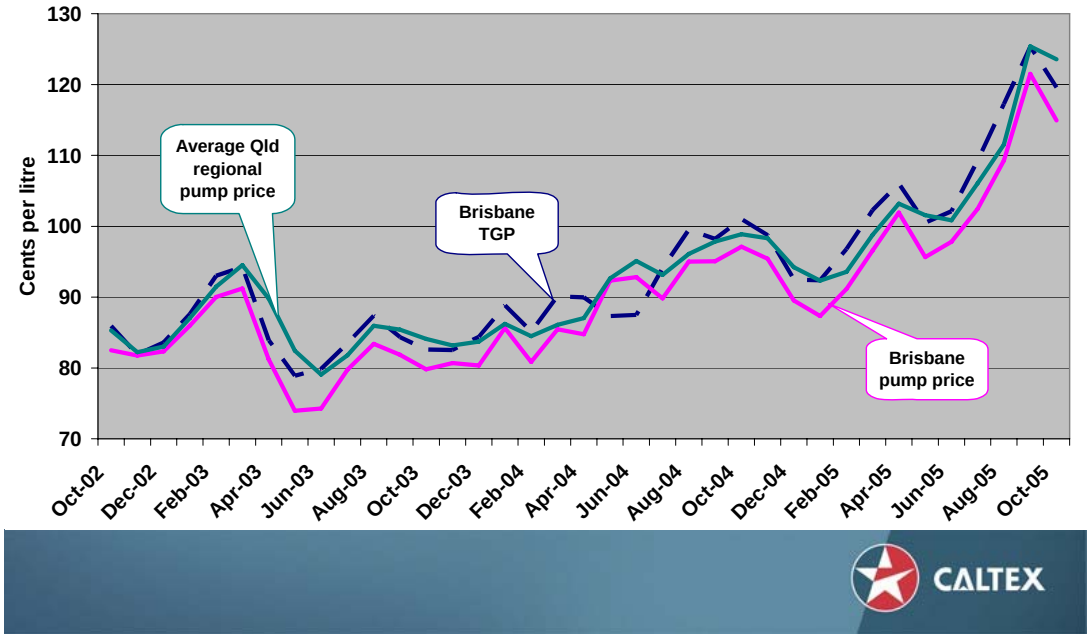


Chart 11 shows a shorter, more recent period from the previous chart, once again for regional prices. The pattern of response here is quite different from Brisbane. Regional prices on average matched the increase in Singapore prices but not the decrease. In fact, in the second week after Katrina, regional prices increased rather than decreasing with Singapore prices. The sign of the change was correct in the third week but the amplitude less (consistent with history) and in the following weeks the changes were fairly well matched. This meant that on a cumulative basis, country prices stayed relatively high against Singapore prices rather than falling as for Brisbane prices. This stimulated considerable public comment.

However, Chart 12 puts the regional and Brisbane prices in context.

Chart 12

Regional and metro pump prices



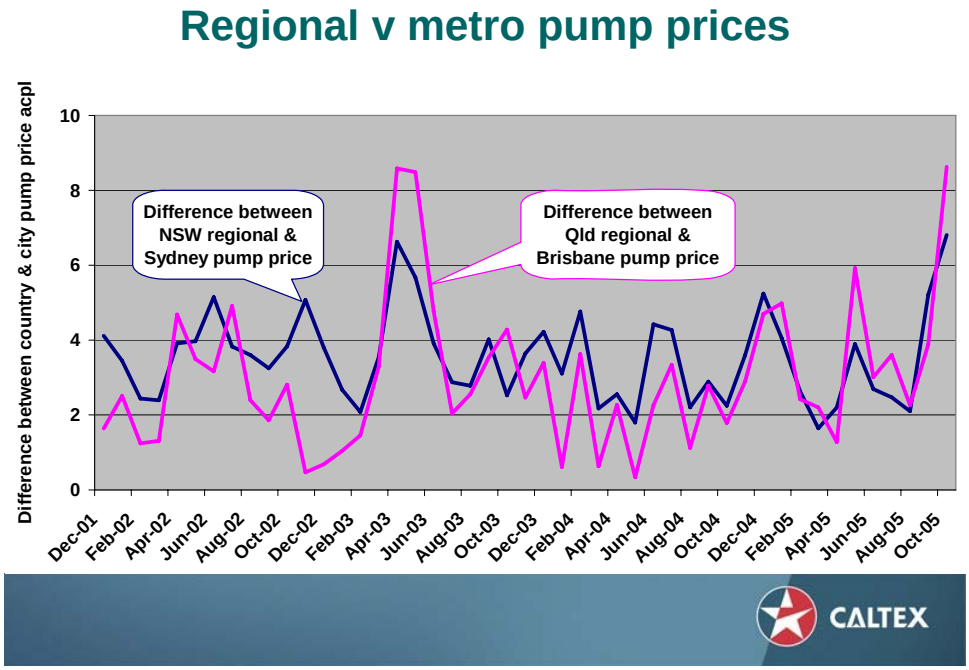
Caltex's terminal gate price (TGP) closely tracks Singapore prices and Brisbane prices very closely track TGP. The same close tracking would show if Brisbane prices were charted against MOPS95 plus freight. However, close examination of the regional pump price line shows that on every occasion that Brisbane prices decrease, the margin between regional and Brisbane prices increases, for up to 3 months. When Brisbane prices increase, the margin is greatly decreased. The increase in the regional/city pump price margin post-Katrina, which is also an increase in the regional pump price relative to Singapore prices, is consistent with this earlier experience. Over time, prices average out and the regional/Brisbane relationship is highly correlated, as shown on the chart. No one is getting "gouged" and there is no "profiteering".

Caltex can't offer a definitive explanation for regional pump price behaviour as we operate very few sites in the country (see Table 1). However, a plausible explanation is as follows. There is less competition in regional and rural areas than in Brisbane/Gold Coast and major supermarket chains have a strong presence. While benefiting motorists through lower prices, supermarket chains have built volume at the expense of smaller, typically independent, service stations and they also have a stated policy of pricing against the lowest competitor in a country town. As a consequence, the volume gained by any non-supermarket service station from discounting could be short-lived as a result of the pricing responses of competitors, so the net result of discounting could be no volume gain but a reduction in retail margin. For this reason, pump prices, through normal competitive forces, are likely to be "sticky" downwards with a consequent increase in retail margins.

Similarly, when Singapore prices fall, hence wholesale prices (the two are typically rigidly linked), pump prices follow more slowly than in the city. A similar effect occurs when wholesale prices increase as a result of increasing Singapore prices – an individual retailer cannot raise pump prices easily with loss of volume, so retail margins are compressed.

Chart 13 shows, for NSW and Queensland, the difference between the average regional pump price and metro price.

Chart 13



For NSW, there is no long term trend. For Queensland, the same is probably true but the difference was depressed in 2004, probably due to the introduction of supermarket and United sites, and the Hurricane Katrina-induced retail margin increase, which on past experience will dissipate by year end.

Overall, the charts show that recent fuel price increases are the result of competition and short term trends reflect those experienced in the past. There are no grounds for concern and no case for increased ACCC powers or regulation.

Regulatory arrangements in Australia

A number of regulatory schemes have been implemented or considered nationally or in other states. Some of this regulation has been removed because it proved ineffective or even counter-productive. For example wholesale price surveillance (setting of maximum wholesale prices) by the ACCC was removed in 1998.

Western Australia has implemented various kinds of regulation of the petroleum market, including retail price control (the FuelWatch scheme), wholesale price regulation of terminal gate prices and so-called 50-50 legislation affecting tied supply arrangements. Victoria regulates wholesale prices.

Caltex's view is these arrangements are ineffective at best and at worst anti-competitive, for example WA FuelWatch. We are opposed to all such regulation as against the interests of consumers and industry and this view is generally shared by the ACCC.

If some degree of regulation is considered necessary, the proposed Australian Government Oilcode, a mandatory code of practice under the Trade Practices Act, contains an appropriate framework for price transparency and access to supply. Caltex supports the Oilcode as part of a market reform package including repeal of the Sites and Franchise Acts. Caltex can provide the inquiry with a draft Oilcode on request and explain the pricing and supply provisions. Alternatively, the Department of Industry, Tourism and Resources would no doubt be pleased to provide this information.

In this section, Caltex provides commentary on existing regulatory schemes.

The 24 hour rule and FuelWatch – Western Australia

In January 2001 the Western Australian Government introduced legislation around fuel pricing in an attempt to promote greater price transparency in its state, reduce the volatility of metropolitan retail prices and reduce the differential between city and country fuel prices.

The government introduced a system commonly known as the 24 hour rule whereby retailers in Western Australia must provide information to the Department of Consumer and Employment Protection by 2pm each day about the prices that will apply for the following day's trading. Retail prices must remain at the stated level for the full 24 hours to which they apply (6am – 6am). Prices are made available to consumers on the FuelWatch website the afternoon prior to the period in which they apply. There are penalties for non-compliance.

The theory behind the 24 hour rule was that increased transparency would allow consumers to easily identify where to buy the cheapest fuel and an inability to change prices frequently would make retailers more cautious about the board prices they set.

Unfortunately the results of the Western Australian Government's regulation have been contrary to those it hoped to achieve.

For consumers, the anti-competitive nature of the 24 hour rule is more likely to lead to higher average fuel prices than would be the case in absence of the rule. In other metropolitan areas in Australia, consumers benefit from intense competition in markets in which retailers continuously discount fuel to respond to local competition, until the discounting can no longer be sustained and prices return to a profitable level. This cannot happen as effectively in Perth.

For site operators, the inability to be flexible with board prices in response to unpredictable daily volumes, as well as local competition, can negatively impact on the viability of that operation.

Independent operators may be forced to leave the market in such an anti-competitive environment.

The administration costs of the program should be taken into account, although to what extent they are offset by fines is unknown.

The ACCC first investigated the 24 hour rule in 2001 and, in its assessment, wrote, "This option is not supported because it is likely to adversely affect independent retailers, which over time could lead to a lessening in the degree of competition, as independent retailers may exit the market. This, in turn, could lead to higher average retail petrol prices."[2]

Their research showed that for the June and September quarters in 2001, average retail petrol prices in Perth were higher than those in Sydney and Melbourne, where their average retail petrol prices had in fact been lower in the previous two quarters.

In a letter to the Hon John Kobelke MP of 9 August 2002, the then ACCC Chairman Professor Allan Fels wrote, "In light of the important role of independents in promoting competition, the ACCC notes with concern the adverse impact of some of the Western Australian fuel arrangements on independents. The 24-hour rule reduces the ability of independents to lower prices during the day to meet their competitors. If they fail to predict the right price for the following day, they are virtually left out of the market for that day, with no benefit to their business or consumers. This is especially a problem for the smaller independent operators who cannot average their returns across a number of sites unlike the major oil companies."

In 2001 the ACCC believed, "it is likely that consumers in aggregate benefit overall from price cycles".[3] This opinion was again confirmed in April 2003 when the ACCC wrote of the 24 hour rule,

[2] *Reducing fuel price variability*, Australian Competition and Consumer Commission 2001, December 2001, p 72
[3] *Reducing fuel price variability*, Australian Competition and Consumer Commission 2001, December 2001, p 4

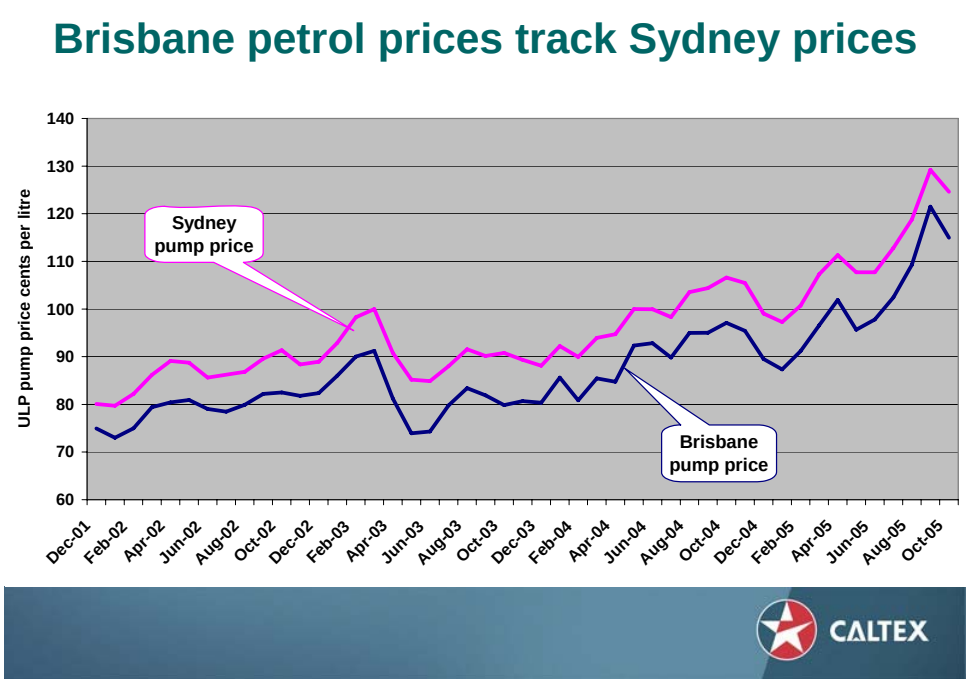
"it is likely to have reduced rather than increased competition because it adversely affected independent operators".[4]

Terminal gate price (TGP) regulation – Western Australia and Victoria

In both cases, the regulation adds administrative costs and risks of fines for accidental non-compliance. In Victoria, the TGP regulation also risks distorting the market to the disadvantage of suppliers. In both cases, the proposed Oilcode regulation could replace the state regulation and should do so.

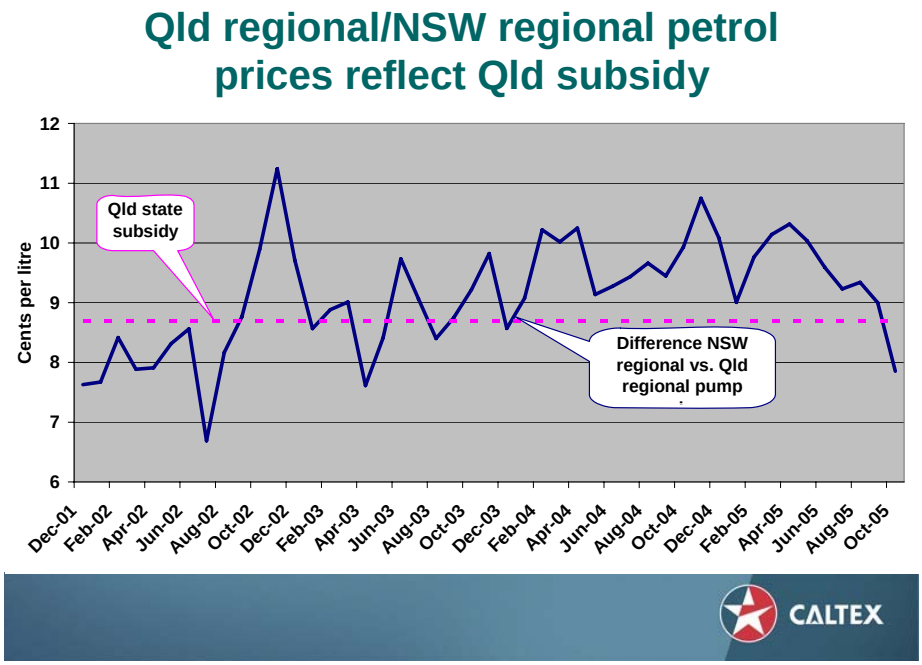
(g) Identify whether Queensland motorists are receiving the full benefit of the 8.354 cpl subsidy and examine the efficiency of administration of the bulk end users scheme.

Chart 14



[4] Australian Competition & Consumer Commission News Release, *ACCC concerned some petrol pricing arrangements lead to higher retail prices*, 23 April 2003

Chart 15



The pass-on of the Queensland subsidy by retailers can be assessed by comparing Sydney and Brisbane pump prices. Chart 14 shows that Brisbane pump prices track Sydney prices very closely. This relationship is illustrated more clearly in Chart 15, which shows the difference between Sydney and Brisbane pump prices. If all other factors were the same (in particular, local competition), the Sydney price would be 9.2 cpl higher than the Brisbane price (8.36 cpl plus GST), shown by the dotted line. The data is remarkably close to this reference line, strongly suggesting the subsidy is being passed on in full through the price at the pump.

Chart 16

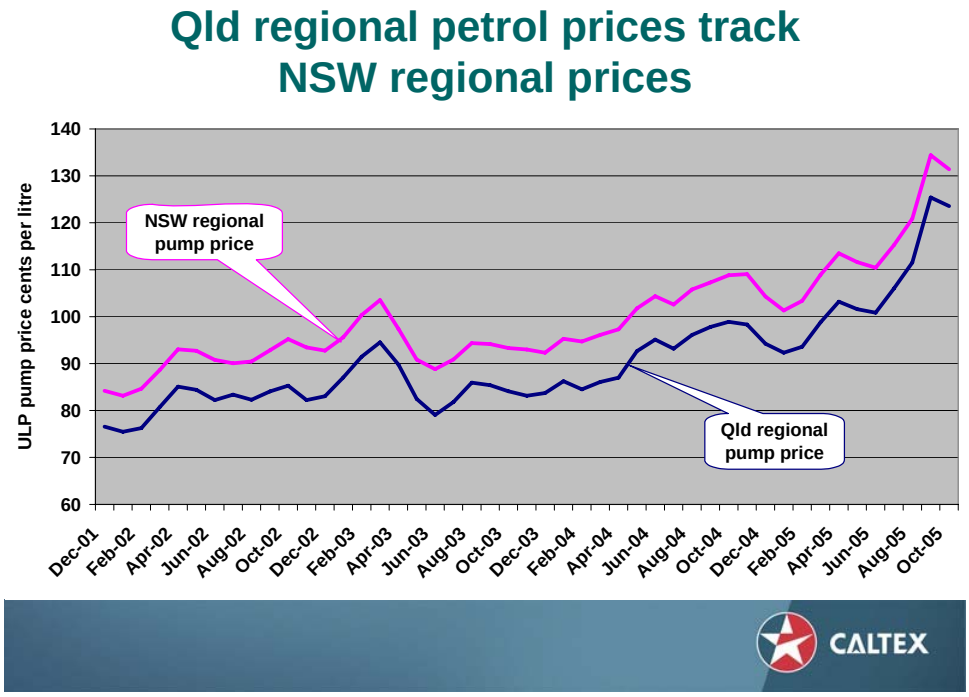


Chart 17

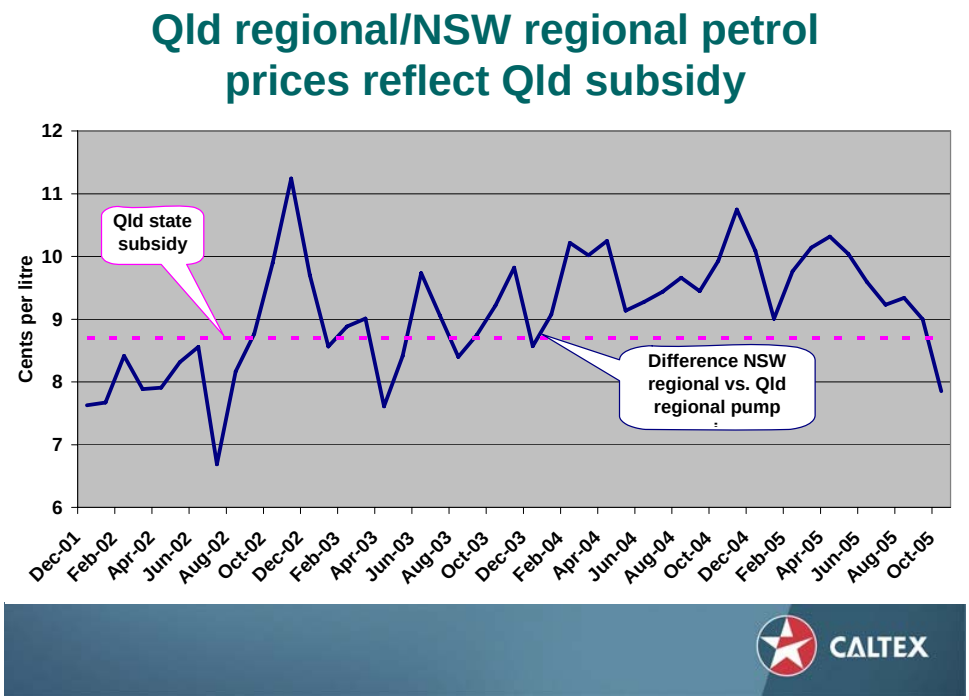


Chart 16 shows the relationship of average regional prices in NSW and Queensland. Chart 17 shows this as a difference. The reference line is set at 8.7 cpl as some of the NSW regional towns have subsidies, so the average difference expected would be less than 9.2 cpl. As for metro areas, the data strongly suggests the subsidy is being passed on in full.

“CONFIDENTIAL APPENDIX”

(Note: confidential data has been deleted – remaining information may be released)

Caltex submission to Queensland Parliament Impact of Petrol Pricing Select Committee

In this public version of Caltex’s submission, confidential data has been deleted but information on the pricing methodology has been retained.

Appendix to Caltex submission to Queensland Parliament Impact of Petrol Pricing Select Committee

The calculations in this appendix are actual calculations that Caltex has made in the course of business using real data. Their purpose is to illustrate how buy-sell prices and Caltex Reference Prices (CRPs) are calculated. The buy-sell price, calculated daily, is the bulk supply price into a fuel storage terminal. The CRP is the ruling wholesale price (ie the list price) for a product supplied to a wholesale customer, excluding delivery. It has bundled into it charges that relate to both fuel and services (eg credit, brand, site rental but not delivery) so is different in concept from Caltex's terminal gate prices, which are for supply of fuel at the terminal loading rack into a road tanker for cash.

Table A1

Indicative Brisbane 2H05 buy/sell price for ULP excluding excise and GST

Assumed Density (L/T)	1356	
Assumed Density (BBLS/T)	8.5	
MOPS 95 (daily spot)	USD/bbl	
Quality Premium	USD/bbl	
subtotal	USD/bbl	
Exchange Rate (daily spot)	USD/AUD	
FREIGHT & WHARFAGE		
Worldscale (WS)	USD/t	
Platts WS index		
Freight	USD/bbl	
Insurance&Loss (%)		
I&L	USD/bbl	
Wharfage	AUD/kL	
Wharfage	USD/bbl	
subtotal	USD/bbl	
Total Price	USD/bbl	
Total Price	ACPL	

Table A2

Indicative Brisbane 2H05 buy/sell price calculation for diesel excluding excise and GST

Assumed Density (L/T)	1209	
Assumed Density (BBLS/T)	7.6	
MOPS ADO 0.05% (daily spot)	USD/bbl	
Quality Premium	USD/bbl	
subtotal	USD/bbl	
Exchange Rate (daily spot)	USD/AUD	
FREIGHT & WHARFAGE		
Worldscale	USD/t	
Platts WS index		
Freight	USD/bbl	
Insurance and Loss (%)		
I&L	USD/bbl	
Wharfage	AUD/kL	
Wharfage	USD/bbl	
subtotal	USD/bbl	
Total Price	USD/bbl	
Total Price	ACPL	

Table A3

Indicative Brisbane CRP for ULP excluding excise and GST

Assumed Density (L/T)	1356	
Assumed Density (BBLS/T)	8.5	
MOPS95 7 day rolling Average	USD/bbl	
Quality Premium	USD/bbl	
subtotal	USD/bbl	
Exchange Rate Rolling Average	USD/AUD	
FREIGHT & WHARFAGE National Average		
Worldscale	USD/t	
Platts	Index	
Freight	USD/bbl	
I&L (%)		
I&L	USD/bbl	
Wharfage	AUD/kL	
Wharfage	USD/bbl	
Subtotal	USD/bbl	
Marketing margin, including terminal and other marketing costs	A cpl	
Total Price	A cpl	

Table A4

Indicative Brisbane CRP calculation for diesel excluding excise and GST

Assumed Density (L/T)	**1209**	
Assumed Density (BBLS/T)	**7.6**	
MOPS ADO 0.05% Rolling Average	USD/bbl	
Quality Premium	USD/bbl	
subtotal	USD/bbl	
Exchange Rate Rolling Average	USD/AUD	
FREIGHT & WHARFAGE National Average		
WS	USD/t	
Platts	Index	
Freight	USD/bbl	
I&L (%)		
I&L	USD/bbl	
Wharfage National Average	AUD/kL	
Wharfage	USD/bbl	
Subtotal	USD/bbl	
Marketing margin, including terminal and other marketing costs	A cpl	
Total Price	ACPL	

Table A5

What is the Caltex Reference Price?

- Caltex Reference Price (CRP) is Caltex's ruling wholesale price.
- Caltex calculates the CRP for petrol and diesel on a daily basis.
- The Caltex Reference Price is based on the concept of import parity and uses Singapore prices (USD/bbl) for product trading, as a marker.
- To reduce price variability and for ease of administration, CRP is changed only if the calculated price movement is greater or less than 0.45 cpl.
- Utilisation of seven day rolling averages for pricing factors such as MOPS and exchange rates to reduce price volatility.

Caltex Ruling Wholesale Price Petrol

- Adjusted Singapore Spot Price (USD/BBL) ie for ULP we use MOPS 95 and add to it the National Quality Premium US$XX /BBL
- Seven day rolling average price converted from USD/BBL to ACPL (Price of Basket)
  + Insurance factor *(Price of Basket + Weighted average freight)
  + Weighted average wharfage
  + Marketing margin, including terminal and other marketing costs
  = National Base Price
  + Excise
  - State subsidy (where applicable NB. Qld subsidy is at retail level, not wholesale)
  + State quality premium (where applicable)
  = CRP (excl GST)
  + 10%GST
  = Caltex Reference Price (or Caltex's ruling wholesale price including GST).

Caltex Ruling Wholesale Price Diesel

- Adjusted Singapore Spot Price (USD/BBL) ie for Low Sulfur Diesel we use 100% Gasoil 0.05% S and add to it the National Quality Premium $US XX/BBL
- Seven day rolling average price converted from USD/BBL to ACPL (Price of Basket)
  + Insurance factor *(Price of Basket + Weighted average freight)
  + Weighted average wharfage
  + Marketing margin, including terminal and other marketing costs
  = National Base Price
  + Excise
  - State Subsidy (where applicable)
  + State quality premium (if applicable)
  = CRP (excl GST)
  + 10%GST
  = Caltex Reference Price (or Caltex's ruling wholesale price including GST).